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ROTHMANS OF PALL MALL CANADA LIMITED ANNUAL REPORT 1968



Rothmans
THE GREATEST NAME
IN CIGARETTES

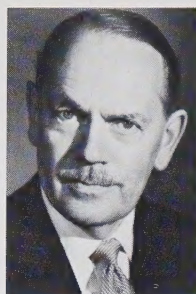
ROTHMANS OF PALL MALL CANADA LIMITED
ANNUAL REPORT 1968

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Directors



JOHN H. DEVLIN, TORONTO
PRESIDENT
ROTHMANS OF PALL MALL
CANADA LIMITED



SIR FRANCIS DE GUINGAND,
K.B.E., C.B., D.S.O.
LONDON, ENG.
CHAIRMAN
CARRERAS LIMITED



CHARLES F. W. BURNS, KING, ONT.
CHAIRMAN
BURNS BROS. AND DENTON LIMITED



JOEL W. ALDRED, TORONTO
PRESIDENT
JOEL W. ALDRED LIMITED



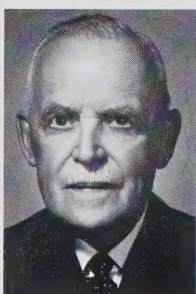
SHIRLEY G. DIXON, O.B.E., Q.C.,
MONTREAL
FORMERLY VICE PRESIDENT
THE ROYAL TRUST COMPANY



HAROLD S. FOLEY, VANCOUVER
PRESIDENT
SCANLON HOLDINGS LIMITED



CHARLES A. MASSEY, TORONTO
FORMERLY PRESIDENT
LEVER BROTHERS LIMITED



RT. HON. LOUIS S. ST-LAURENT,
Q.C., LL.D., P.C.
QUEBEC, P.Q.
PARTNER—ST-LAURENT, MONAST,
DESMEULES & WALTERS



JOHN E. SHAFFNER,
PORT WILLIAMS, N.S.
PRESIDENT
M. W. GRAVES & CO. LTD.



WILMAT TENNYSON, TORONTO
VICE PRESIDENT MARKETING
ROTHMANS OF PALL MALL
CANADA LIMITED

Officers

Chairman of the Board

THE RIGHT HONOURABLE
LOUIS STEPHEN ST-LAURENT, Q.C., LL.D., P.C.

President

JOHN HERBERT DEVLIN

Vice President Marketing

WILMAT TENNYSON

Vice President Finance and Treasurer

PAUL JACOBUS ERASMUS

Vice President and Secretary

ROBERT HOWIE HAWKES

Vice President Production

DANIEL DI IANNI

Vice President Personnel and Industrial Relations

GEORGE STEWART

Vice President Sales

ROBERT THOMAS LLOYD

Vice President Advertising

ROY HENRY NEWTON

Directors' Report

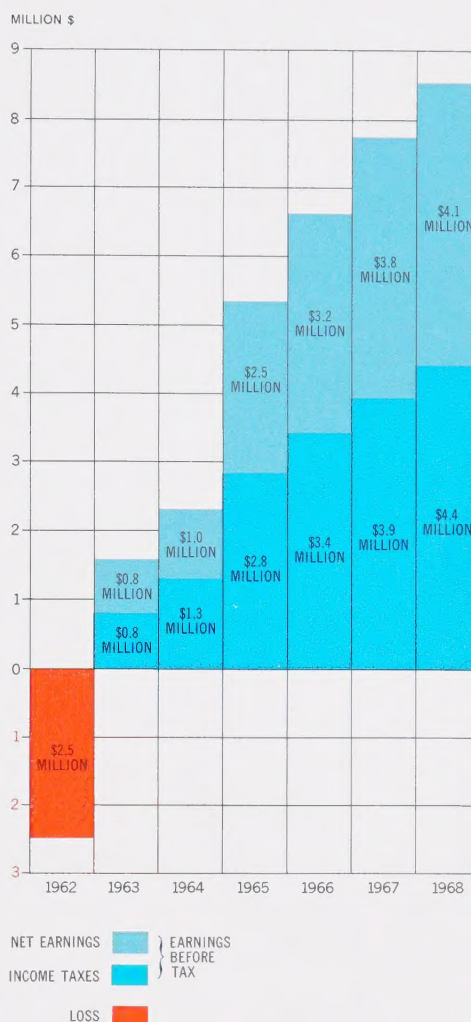
For the sixth consecutive year, your Company has set new records for sales and earnings. Sales increased from \$166,014,000 to \$173,640,000, an increase of 4.6 percent. Net earnings increased from \$3,763,000 to \$4,070,000, an increase of 8.2 percent.

Earnings per share were \$2.54 compared to \$2.35 for the previous year. In 1967, the reported earnings of \$2.89 per share were based on 1,300,000 shares outstanding. On June 30, 1968, the 300,000 Class B Convertible Deferred shares were converted into Common shares, thereby increasing the number of Common shares from 1,300,000 to 1,600,000. (See Note 7 to the Financial Statements on Page 15.)

FINANCIAL YEARS ENDED JUNE 30	1968	1967	INCREASE
SALES	\$173,640,000	\$166,014,000	4.6%
EARNINGS:			
Before Taxes	8,475,000	7,712,000	9.9%
Net	4,070,000	3,763,000	8.2%
Per Common Share			
1,600,000 Shares	\$2.54	\$2.35	8.2%

Earnings Before Tax and Net Earnings

FINANCIAL YEARS ENDED JUNE 30



Your Company announced its initial dividend on April 2, 1968. The first dividend of 25 cents was paid on June 17, 1968. Your Board expressed the intention at that time to maintain an annual dividend rate of \$1.00 per share payable on a quarterly basis.

In early January, \$15,000,000 in long-term funds were raised through the issue of 7½ percent Sinking Fund Debentures, Series A, to mature January 3, 1988. Each \$1,000 debenture carried a warrant to purchase 10 Common shares. The funds derived from this issue were applied against operating bank loans.

On June 6, 1968, your Company purchased 2,400,000 common shares (11 percent) in Canadian Breweries Limited, from Argus Corporation Limited. The purchase price was \$28.8 million, or \$12 per share. The acquisition was made through Rothmans Investments Limited, in which your Company presently has a 50 percent interest. Rothmans of Canada Limited, the Canadian holding company of the Rothmans World Group, holds the other 50 percent interest in Rothmans Investments Limited. Your Company has agreed, subject to obtaining additional long-term financing, to acquire at cost the common shares of Rothmans Investments Limited presently owned by Rothmans of Canada Limited. As outlined in the notice of our Annual Meeting, shareholder approval will be requested to increase the authorized share capital of the Company.

Cigarette sales in Canada have been adversely affected by an unprecedented series of increases in the consumer price since December 1967. Effective December 1, 1967, the Federal Tax was increased from \$5.00 to \$6.00 per thousand cigarettes, or two cents per pack. On December 8, as a result of increased costs, your Company

increased its cigarette selling prices. In the first five months of 1968, five Provinces raised the Provincial tax on cigarettes. The effect of the increases on the price of cigarettes across Canada is highlighted below:

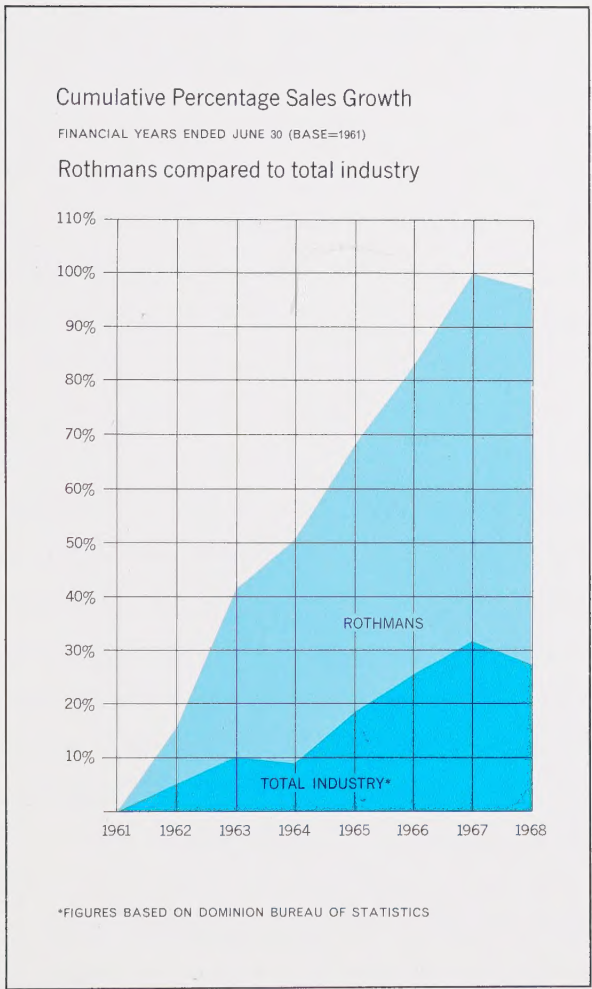
Selling Price of King Size Cigarettes per Pack of 20's

<i>Province</i>	<i>Retail Price July/67</i>	<i>Retail Price July/68</i>	<i>% Increase</i>
British Columbia	41¢	44¢	7.3
Alberta	39¢	42¢	7.7
Saskatchewan	43¢	49¢	14.0
Manitoba	47¢	50¢	6.4
Ontario	41¢	48¢	17.1
Quebec	44¢	50¢	13.6
New Brunswick	43¢	46¢	7.0
Nova Scotia	41¢	44¢	7.3
Prince Edward Island	43¢	50¢	16.3
Newfoundland	46¢	55¢	19.6

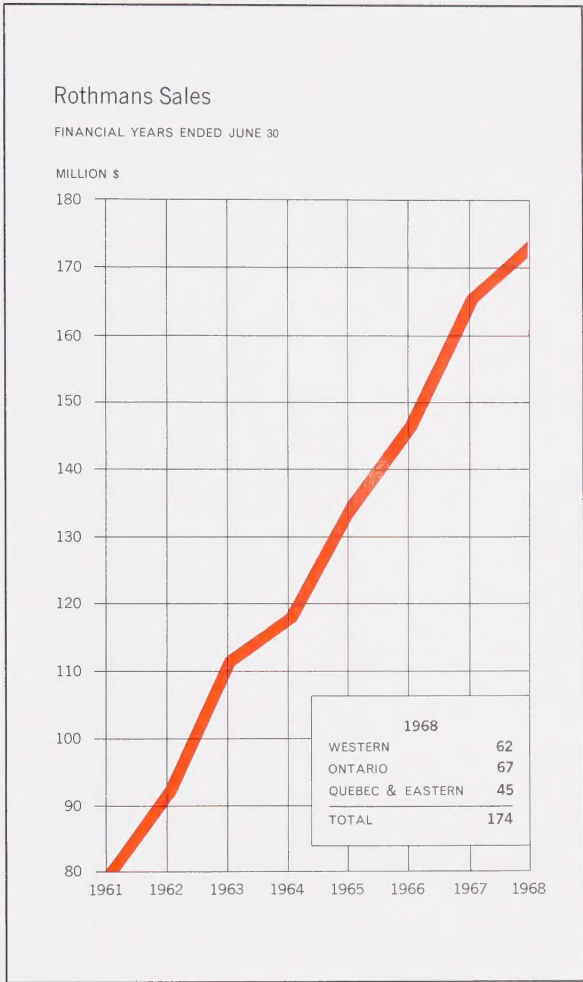
As a result of these substantial price increases, total cigarette sales in Canada declined in the early part of 1968. Total industry cigarette production, as reported by the Dominion Bureau of Statistics, declined by 3.3 percent, from 47,285 million for the twelve-month period ended June 30, 1967, to 45,731 million for the same period in 1968.

Your Company's sales for the year were 10,227 million cigarettes, compared to 10,388 million cigarettes for the previous year; a decrease of 1.5 percent. Industry sales in July, August and September appear to have returned to normal, and your Company's unit cigarette sales for the four months ended October 31, 1968, were higher than in the previous year.

Rothmans share of the total Canadian cigarette market continues to increase.



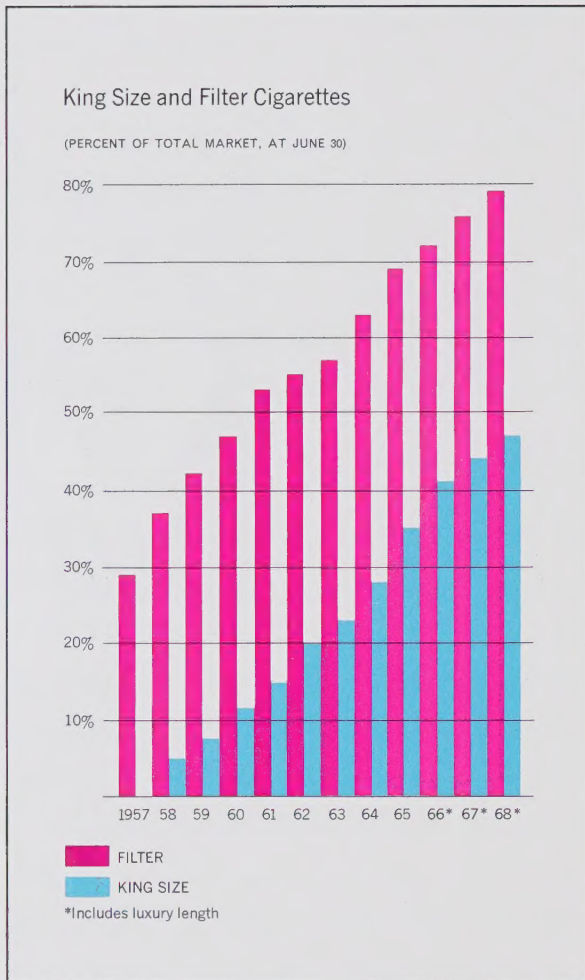
The following chart outlines the eight-year sales history of the Company and a breakdown of regional sales for 1968:



Filter cigarettes continue to increase their share of the total market. Compared to 76 percent of the market a year ago, filter cigarettes now account for 79 percent. King size cigarettes, including luxury length, increased to approximately 47 percent of the total market.

Luxury length cigarettes now represent 3 percent of the total Canadian market. In the United

States, where luxury length cigarettes were first introduced, it appears that these products are now levelling off at approximately 11-12 percent of the total U.S. market.



Rothmans King Size continues to be Canada's largest selling king size brand and increased its sales over the previous year.

Coupon and give-away brands continue to increase their share of the market and now represent approximately 23 percent of the total market.

In this segment of the market, your Company is represented by two brands: Number 7 and the new Sportsman 68 mm. cigarette. Number 7 continues to strengthen and is now the leader in the coupon market in Western Canada. The new Sportsman received outstanding consumer acceptance in the Province of Quebec where it was first introduced in June, and the brand has recently been introduced in the British Columbia market.

The menthol cigarette share of total market remains steady at approximately six percent. Craven "M", your Company's leading menthol brand, continues to increase in sales and share of market.

Your Company's luxury length brands, Dunhill and St. Moritz (menthol), which were "firsts" in the Canadian cigarette market, continue to sell well at a premium price of three cents per pack over king size.

In March 1968, your Company concluded an agreement for the use, under royalty, of the Strickman Filter. In June of this year, Ransom, the world's first king size cigarette with the Strickman Filter, was introduced. Initially, the production capacity for this brand was limited; it is now in almost full distribution across Canada. Ransom has already established its leadership in this segment of the market.

The traditional "one-price cigarette market" in Canada has changed to a multi-price structure.

Cigarettes are now selling at four different prices for short, regular, king size, and luxury length types. Your Company's brands are spread as follows over the four price classes:

Rothmans Brands by Price Class

<u>SHORT</u>	<u>REGULAR</u>	<u>KING SIZE</u>	<u>LUXURY LENGTH</u>
<i>Filter:</i>	<i>Filter:</i>	<i>Filter:</i>	<i>Filter:</i>
Sportsman	Craven "A"	Rothmans	Dunhill
	Black Cat	Number 7	St. Moritz
		Craven King Size	
	<i>Plain:</i>	Peter Stuyvesant	
	Sportsman	Ransom	
	Black Cat	Craven "M"	
		Sportsman	
		Riggio	

The 1967 Ontario flue-cured tobacco crop, which totalled 196 million pounds, was lower than the 220 million pounds originally forecast. However, the average price per pound of 69.1 cents was lower than the 71.4 cents paid for the 1966 crop. Your Company continues to pay above-average prices for its tobacco in order to maintain the highest quality in its products. Prices paid by Rothmans were 73.2 cents per pound for the 1967 crop, compared to 75 cents per pound in the previous year. The acreage allotment for 1968 was 126,700 acres, compared with 138,800 acres allotted in 1967. The 1968 crop is estimated to yield approximately 210 million pounds.

Since 1964, your Company has been buying tobacco in the Maritimes and last year purchased just under 40 percent of the total crop. Our purchases in the Province of Quebec have averaged between 25 and 30 percent of the total crop in that Province.

On December 20, 1967, a two-year labour contract was entered into with the employees in the Toronto factory. In early May, negotiations for a new contract with the Quebec factory broke down and a three-week strike ensued. On May 24, an agreement was reached on a new two-year contract. The basic settlement resulted in wage increases for both factories of 10 percent in the first year and 7 percent in the second year of the contracts.

An expansion of the production areas in Quebec City has been completed with the building of a new warehouse for the storage of raw materials and finished stocks. More advanced cigarette production machinery continues to be installed in the Quebec factory, and this program will be carried forward into the 1968-69 fiscal year.

The Annual and a Special General Meeting of Shareholders will take place on December 18, 1968. The formal notice of meeting, information circular and proxy form are sent with this report.

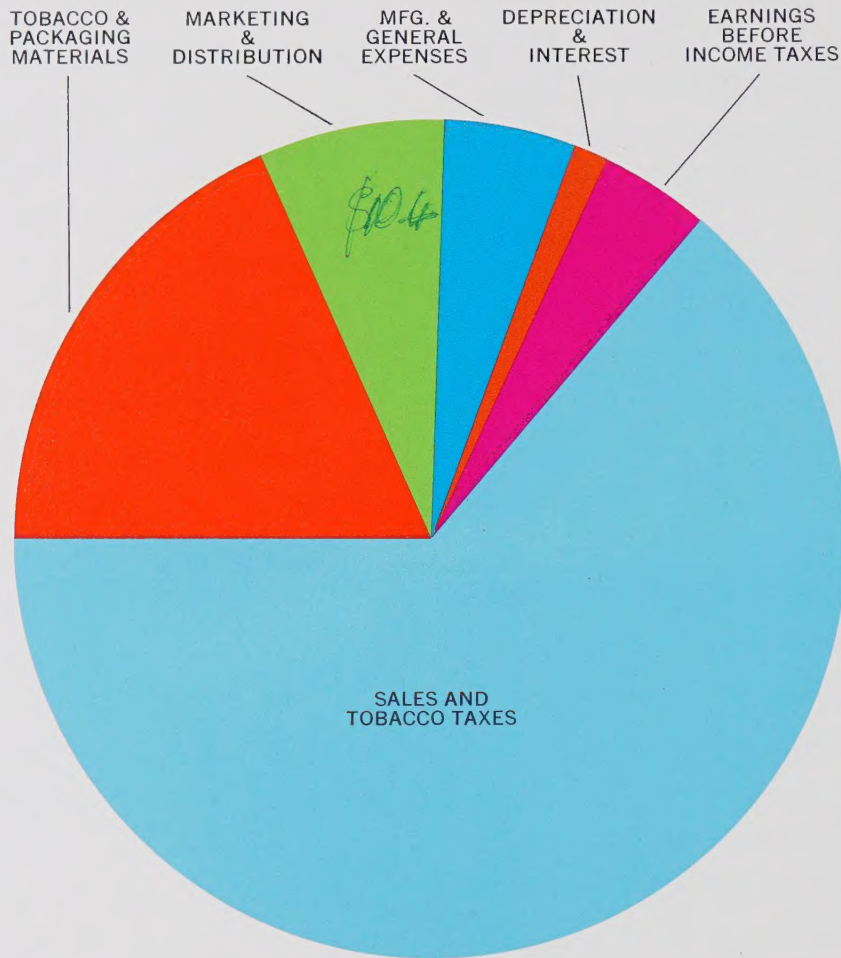
The Board of Directors is grateful for the dedication displayed by all employees and wishes to thank the shareholders for their loyal support.



President

Distribution of Sales Dollar

AS A PERCENT OF TOTAL SALES



FINANCIAL YEARS ENDED JUNE 30						
1968	63.3%	18.1%	6.2%	5.5%	2.0%	4.9%
1967	63.6%	18.3%	6.6%	5.1%	1.8%	4.6%
1966	65.1%	17.6%	6.3%	4.8%	1.7%	4.5%
1965	65.4%	17.2%	6.7%	5.1%	1.7%	3.9%
1964	66.7%	17.5%	6.8%	5.2%	1.9%	1.9%
1963	66.7%	17.7%	7.3%	5.3%	1.6%	1.4%
1962	67.0%	17.1%	11.1%	5.7%	1.8%	2.7%

Seven-Year Financial Review

(in thousands of dollars)

	Financial Years Ended June 30:						
	1968	1967	1966	1965	1964	1963	1962
<i>Operating:</i>							
SALES	\$	\$	\$	\$	\$	\$	\$
Cigarettes - - - - -	169,730	161,887	142,689	130,007	115,051	108,376	88,291
Other tobacco products - - - - -	3,910	4,127	4,387	4,797	4,013	3,877	3,910
Sales - - - - -	173,640	166,014	147,076	134,804	119,064	112,253	92,201
Sales and tobacco taxes - - - - -	109,860	105,609	95,791	88,116	79,356	74,742	61,770
	63,780	60,405	51,285	46,688	39,708	37,511	30,431
EARNINGS							
Earnings—before income taxes - - - - -	8,475	7,712	6,590	5,297	2,308	1,632	2,493
Income taxes - - - - -	4,405	3,949	3,424	2,839	1,302	821	12
Net earnings - - - - -	4,070	3,763	3,166	2,458	1,006	811	2,505
— as a percent of sales - - - - -	2.3%	2.3%	2.2%	1.8%	0.8%	0.7%	2.7%
— as a percent of sales excluding taxes - - -	6.4%	6.2%	6.2%	5.3%	2.5%	2.2%	8.2%
Net earnings per common share - - - - -	\$2.54	\$2.89	\$2.44	\$1.89	\$0.77	\$0.62	\$1.93
Common shares outstanding (in thousands)- -	1,600	1,300	1,300	1,300	1,300	1,300	1,300
DIVIDENDS PAID							
— Per common share - - - - -	\$0.25	—	—	—	—	—	—
CAPITAL EXPENDITURE—NET - - - - -	3,564	2,010	2,142	2,060	1,818	406	385
DEPRECIATION - - - - -	1,634	1,504	1,376	1,226	1,162	1,001	1,025
INTEREST PAID - - - - -	1,911	1,413	1,145	1,133	1,045	804	638
<i>Financial:</i>							
WORKING CAPITAL							
Current assets - - - - -	56,899	57,465	43,744	38,431	32,068	29,945	26,519
Current liabilities - - - - -	40,928	45,194	34,042	32,439	25,772	22,277	19,786
Balance June 30th - - - - -	15,971	12,271	9,702	5,992	6,296	7,668	6,733
Ratio - - - - -	1.39	1.27	1.28	1.18	1.24	1.34	1.34
TOTAL ASSETS							
Current assets - - - - -	56,899	57,465	43,744	38,431	32,068	29,945	26,519
Fixed assets—net - - - - -	9,991	8,061	7,555	6,789	5,955	5,266	5,801
Investments and other - - - - -	12,100	227	44	—	—	172	241
Intangible assets - - - - -	573	3,467	3,452	8,835	10,030	11,235	12,700
Total assets - - - - -	79,563	69,220	54,795	54,055	48,053	46,618	45,261
LOANS AND INDEBTEDNESS							
Debentures - - - - -	15,000	—	—	—	—	—	—
Other indebtedness - - - - -	301	301	301	301	3,424	6,490	7,675
Current bank loans - - - - -	28,809	32,699	25,281	20,358	16,499	15,396	12,831
CAPITAL INVESTED							
Long-term debt and provisions - - - - -	15,051	301	301	301	3,424	6,490	7,675
Shareholders' tangible equity - - - - -	21,877	18,419	15,571	12,480	8,827	6,616	5,100
Total capital invested - - - - -	36,928	18,720	15,872	12,781	12,251	13,106	12,775
— Percent of shareholders' equity							
to capital invested - - - - -	59.2%	98.4%	98.1%	97.6%	72.1%	50.5%	39.9%
TANGIBLE EQUITY PER COMMON SHARE - - - -	\$13.67	\$14.17	\$11.98	\$ 9.60	\$ 6.79	\$ 5.09	\$ 3.92

Consolidated Balance Sheet

ASSETS

	1968	1967
Current Assets:		
<i>Accounts receivable—</i>		
Trade - - - - -	\$ 7,624,000	\$ 7,534,000
Affiliated companies - - - - -	37,000	139,000
Other - - - - -	440,000	361,000
	<u>8,101,000</u>	<u>8,034,000</u>
<i>Inventories, at average cost—</i>		
Leaf tobacco - - - - -	34,257,000	33,480,000
Manufactured stock - - - - -	10,860,000	13,245,000
Packaging material and other (Note 4) - - - - -	2,860,000	2,218,000
	<u>47,977,000</u>	<u>48,943,000</u>
<i>Prepaid expenses - - - - -</i>	<u>821,000</u>	<u>488,000</u>
Total Current Assets - - - - -	<u>56,899,000</u>	<u>57,465,000</u>
Refundable Tax, less current portion - - - - -	<u>100,000</u>	<u>227,000</u>
Investment in Shares and Advances to Rothmans Investments Limited, at cost (Note 1) - - - - -	<u>12,000,000</u>	<u>—</u>
Fixed Assets, at cost (Note 2) - - - - -	<u>20,971,000</u>	<u>17,670,000</u>
<i>Less—Accumulated depreciation - - - - -</i>	<u>10,980,000</u>	<u>9,609,000</u>
	<u>9,991,000</u>	<u>8,061,000</u>
Other Assets:		
Discount and expense on long-term debt - - - - -	444,000	—
Goodwill, at cost (Note 3) - - - - -	—	3,338,000
Trademarks, at cost - - - - -	129,000	129,000
	<u>573,000</u>	<u>3,467,000</u>

APPROVED ON BEHALF OF THE BOARD:

JOHN H. DEVLIN, *Director*

JOEL W. ALDRED, *Director*

\$79,563,000 \$69,220,000

Sheet—June 30, 1968

LIABILITIES

	1968	1967
Current Liabilities:		
Bank loans (secured) - - - - -	\$28,809,000	\$32,699,000
Accounts payable and accrued - - - - -	3,872,000	2,834,000
Income taxes - - - - -	2,003,000	3,542,000
Excise, sales and other taxes - - - - -	5,994,000	6,119,000
Current portion of long-term debt - - - - -	250,000	—
Total Current Liabilities - - - - -	<u>40,928,000</u>	<u>45,194,000</u>
Long-Term Debt , less amount due within one year included in current liabilities (Note 5) - - - - -	14,750,000	—
Provision for Retirement Annuities - - - - -	301,000	301,000
	<u>55,979,000</u>	<u>45,495,000</u>
Deferred Income Taxes (Note 6) - - - - -	1,134,000	939,000

SHAREHOLDERS' EQUITY

Capital Stock (Note 7):

Authorized—

2,100,000 common shares without nominal or par value

180 Class A Redeemable Deferred shares of a par value of \$10,000 each

300,000 Class B Convertible Deferred shares without nominal or par value

Issued—

Common shares—1,600,000 (1967—1,300,000) - - - - - 16,000,000 13,000,000

Class A shares—Nil (1967—90) - - - - - — 900,000

Class B shares—Nil (1967—300,000) - - - - - — 3,000,000

16,000,000 16,900,000

Retained Earnings (Note 8) - - - - - 6,450,000 5,886,000

22,450,000 22,786,000

\$79,563,000 \$69,220,000

ROTHMANS OF PALL MALL CANADA LIMITED

(incorporated under the Canada Corporations Act on May 8, 1956)

AND SUBSIDIARY COMPANIES

Consolidated Statement of Earnings

FOR THE YEAR ENDED JUNE 30, 1968

	1968	1967
Sales - - - - -	\$173,640,000	\$166,014,000
Costs:		
Sales and tobacco taxes - - - - -	109,860,000	105,609,000
Tobacco and packaging materials - - - - -	31,516,000	30,372,000
Manufacturing and general expenses - - - - -	9,533,000	8,450,000
Marketing and distribution expenses - - - - -	10,711,000	10,954,000
Depreciation (Note 2) - - - - -	1,634,000	1,504,000
Interest (Note 9) - - - - -	1,911,000	1,413,000
	<u>165,165,000</u>	<u>158,302,000</u>
Earnings for the year before income taxes - - - - -	8,475,000	7,712,000
Income taxes (Note 6) - - - - -	4,405,000	3,949,000
Earnings for the year - - - - -	<u>\$ 4,070,000</u>	<u>\$ 3,763,000</u>

Consolidated Statement of Retained Earnings

FOR THE YEAR ENDED JUNE 30, 1968

	1968	1967
Balance at beginning of the year - - - - -	\$ 5,886,000	\$ 2,123,000
Earnings for the year - - - - -	4,070,000	3,763,000
Spare parts inventory, less related income taxes (Note 4) -	157,000	—
	<u>10,113,000</u>	<u>5,886,000</u>
Dividend - - - - -	325,000	—
Goodwill written off (Note 3) - - - - -	3,338,000	—
	<u>3,663,000</u>	<u>—</u>
Balance at end of the year - - - - -	<u>\$ 6,450,000</u>	<u>\$ 5,886,000</u>

ROTHMANS OF PALL MALL CANADA LIMITED

(incorporated under the Canada Corporations Act on May 8, 1956)

AND SUBSIDIARY COMPANIES

Consolidated Statement of Changes in Working Capital

FOR THE YEAR ENDED JUNE 30, 1968

	1968	1967
<i>Working capital was increased by:</i>		
Earnings for the year - - - - -	\$ 4,070,000	\$ 3,763,000
Add—Expenses not involving a current outlay of funds—		
Depreciation (Note 2) - - - - -	1,634,000	1,504,000
Deferred income taxes (Note 6) - - - - -	195,000	410,000
Funds from operations - - - - -	5,899,000	5,677,000
Issue of long-term debt, less current portion - - - - -	14,750,000	—
Spare parts inventory, less related income taxes (Note 4) -	157,000	—
Refundable tax - - - - -	127,000	—
	<u>20,933,000</u>	<u>5,677,000</u>
<i>Working capital was decreased by:</i>		
Investment in shares and advances to Rothmans Investments Limited (Note 1) - - - - -	12,000,000	—
Fixed asset acquisitions—net - - - - -	3,564,000	2,010,000
Redemption of Class A shares - - - - -	900,000	900,000
Discount and expense on long-term debt - - - - -	444,000	—
Dividend - - - - -	325,000	—
Refundable tax - - - - -	—	183,000
Trademarks - - - - -	—	15,000
	<u>17,233,000</u>	<u>3,108,000</u>
Increase in working capital - - - - -	3,700,000	2,569,000
Working capital at beginning of the year - - - - -	12,271,000	9,702,000
Working capital at end of the year - - - - -	<u>\$15,971,000</u>	<u>\$12,271,000</u>
Current assets - - - - -	\$56,899,000	\$57,465,000
Current liabilities - - - - -	40,928,000	45,194,000
Working capital - - - - -	<u>\$15,971,000</u>	<u>\$12,271,000</u>

Notes to Financial Statements

JUNE 30, 1968

1. Investment in shares and advances to Rothmans Investments Limited:

Rothmans Investments Limited was incorporated on April 4, 1968. On June 6, 1968, it acquired 2,400,000 shares (11%) of Canadian Breweries Limited for a total consideration of \$28,800,000. The common shares of Rothmans Investments Limited are owned 50% by Rothmans of Pall Mall Canada Limited and 50% by Rothmans of Canada Limited. (Rothmans of Pall Mall Canada Limited has agreed, subject to obtaining additional long-term financing, to acquire at cost the common shares of Rothmans Investments Limited presently owned by Rothmans of Canada Limited.) In addition, both companies have made advances, in the form of income debentures, to Rothmans Investments Limited.

2. Fixed assets and depreciation:

	1968		1967	
	Assets	Accumulated depreciation	Assets	Accumulated depreciation
Land - - - - -	\$ 1,060,000	\$ —	\$ 209,000	\$ —
Buildings - - - - -	3,284,000	1,406,000	2,786,000	1,329,000
Machinery - - - - -	14,561,000	8,800,000	12,765,000	7,642,000
Motor vehicles - - - - -	727,000	327,000	624,000	311,000
Leasehold improvements - - - - -	1,339,000	447,000	1,286,000	327,000
	<u>\$20,971,000</u>	<u>\$10,980,000</u>	<u>\$17,670,000</u>	<u>\$9,609,000</u>

Depreciation has been recorded generally using the diminishing balance method at the rates normally allowed for federal tax purposes.

Capital expenditures for the year ending June 30, 1969 are expected to aggregate \$3,500,000.

Rentals payable under lease agreements approximate \$330,000 annually. Of this amount \$205,000 is committed for a term of not more than three years and the remainder for an average term of ten years.

3. Goodwill:

The goodwill of \$3,338,000 at June 30, 1967 arose from the acquisition of the total capital stock of Rock City Tobacco Company (1960) Limited. Of this amount, \$3,000,000 was represented by the Class B Convertible Deferred shares. During the year ended June 30, 1968, the goodwill was written off against retained earnings.

4. Spare parts inventory:

Prior to July 1, 1967, it was the Company's practice to charge machine spare part purchases directly to earnings. On July 1, 1967, the inventory of parts on hand was recorded on the Company's books at \$330,000 and credited to retained earnings, less the related income taxes of \$173,000. Earnings for the year ended June 30, 1968 have been charged with actual usage. The effect of this change on 1968 earnings was not material.

5. Long-term debt:

On January 3, 1968 the Company received the proceeds of an issue of \$15,000,000 principal amount of 7½% Sinking Fund Debentures, Series A, due January 3, 1988, carrying warrants to purchase common shares on the basis of 10 shares for each \$1,000 principal amount of debentures. Warrants are exercisable at a price of \$25.00 per common share to January 3, 1973 and at a price of \$27.50 per common share thereafter to January 3, 1978. Under the Trust Indenture securing the issue of debentures, the Company is required to make sinking fund payments on or before January 3 in each of the years 1969 to 1987 inclusive, as follows: 1969-1971—\$250,000; 1972-1987—\$800,000. The balance of \$1,450,000 principal amount is due on maturity at January 3, 1988.

A further condition under the Trust Indenture requires that the companies maintain consolidated working capital of an amount not less than the aggregate principal amount of Series A Debentures outstanding.

NOTES TO FINANCIAL STATEMENTS (*Continued*)

6. Deferred income taxes:

Since the Company can claim more depreciation for tax purposes than was recorded in the accounts, estimated income taxes payable in 1968 are less than the amount charged against earnings. This reduction, amounting to \$195,000, has been included in the total of \$1,134,000 set aside on the balance sheet as deferred income taxes.

7. Capital stock:

By supplementary letters patent dated October 14, 1967 the authorized capital stock of the Company was increased by the creation of an additional 500,000 common shares without nominal or par value.

Of the authorized and unissued common shares, 150,000 shares are reserved for possible exercising of warrants issued with the 7½% Sinking Fund Debentures, Series A.

In accordance with their terms of issue, 90 Class A shares were redeemed by December 31, 1966 and the remaining 90 shares were redeemed by December 31, 1967.

The Class B Convertible Deferred shares were convertible at one time, but not from time to time, upon the basis of one Class B share for one common share. These shares were only eligible for conversion to the extent of designated funds, defined as consolidated earnings in excess of \$780,000 per annum computed on a cumulative basis commencing with the fiscal year in which the balance of Class A shares were redeemed. When designated funds reached \$3,000,000, the whole of the issue was to be converted. Inasmuch as all the Class A shares were redeemed by December 31, 1967, the accumulation of designated funds commenced on July 1, 1967. As consolidated earnings for the year ended June 30, 1968 exceeded the requirements for designated funds, the 300,000 Class B shares with a value of \$3,000,000 were converted into 300,000 common shares at June 30, 1968.

8. Retained Earnings:

Retained earnings include \$1,800,000 which was designated as capital surplus on the redemption of 180 Class A shares, including \$900,000 designated on the redemption of 90 shares by December 31, 1967.

Under the Trust Indenture securing the issue of Series A Debentures, the Company cannot declare dividends unless, immediately after giving effect to such action, consolidated retained earnings of the companies will be not less than \$2,548,000.

9. Interest Expense:

Interest expense includes the following:

	1968	1967
Bank loans (operating) - - - - -	\$1,281,000	\$1,413,000
Debentures - - - - -	562,000	—
Bank loan (investment) - - - - -	68,000	—
	<u>\$1,911,000</u>	<u>\$1,413,000</u>

10. Remuneration of Directors:

Total remuneration of directors during the year ended June 30, 1968, in their capacity as directors or officers, amounted to \$231,000 (1967—\$214,000).

AUDITORS' REPORT

TO THE SHAREHOLDERS OF ROTHMANS OF PALL MALL CANADA LIMITED:

We have examined the consolidated balance sheet of Rothmans of Pall Mall Canada Limited and subsidiary companies as at June 30, 1968 and the consolidated statements of earnings, retained earnings and changes in working capital for the year then ended. Our examination included a general review of the accounting procedures and such tests of the accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at June 30, 1968 and the results of their operations and the changes in working capital for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent in all material respects with that of the preceding year.

TORONTO, July 29, 1968.

PRICE WATERHOUSE & CO., *Chartered Accountants.*

Financial

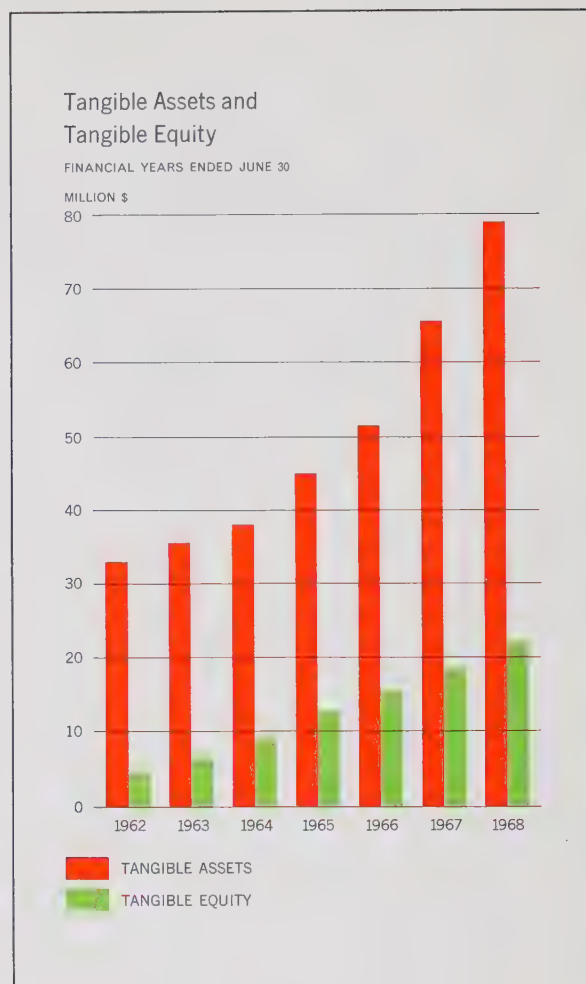
As outlined in the seven-year financial review on Page 9, your Company continues to show substantial growth in both sales and earnings. Net sales, exclusive of sales and tobacco taxes, have more than doubled, from \$30,431,000 in 1962 to \$63,780,000 in 1968. Pre-tax earnings over the period have shown an improvement of some \$11 million, from a loss of \$2,493,000 in 1962, to earnings before tax of \$8,475,000 in 1968.

FINANCIAL POSITION

Shareholders' Equity

Common shareholders' tangible equity increased during the year from \$18,419,000 to \$21,877,000, and now represents \$13.67 per Common share.

As outlined in the Financial Statements, your Company wrote off goodwill amounting to \$3,338,000 against retained earnings at June 30, 1968. The goodwill arose from the acquisition in 1963 of the total capital stock of Rock City Tobacco Company (1960) Limited. Of this amount, \$3,000,000 was represented by the Class



B Convertible Deferred shares. These shares were converted into Common shares as of June 30, 1968. (See Notes 3 and 7 to the Financial Statements on Pages 14 and 15.)

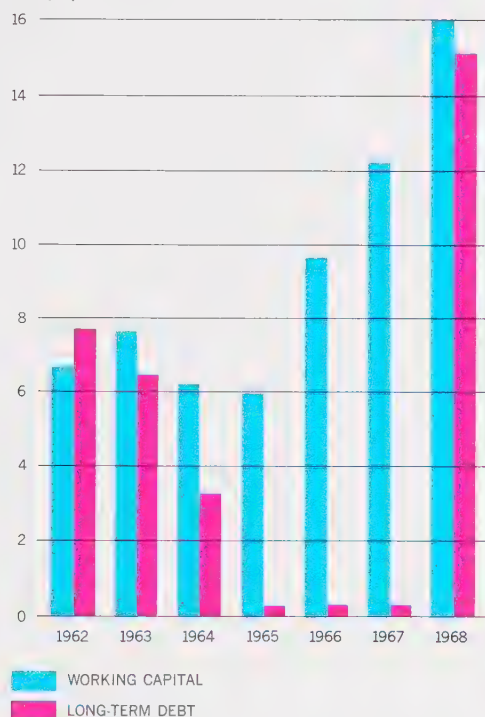
Working Capital

Working capital during the year increased by \$3,700,000, from \$12,271,000 to \$15,971,000. The change in working capital takes into account the issue of \$15,000,000 debentures on January 3, 1968, as well as the investment of \$12,000,000 in

Working Capital and Long-Term Debt

FINANCIAL YEARS ENDED JUNE 30

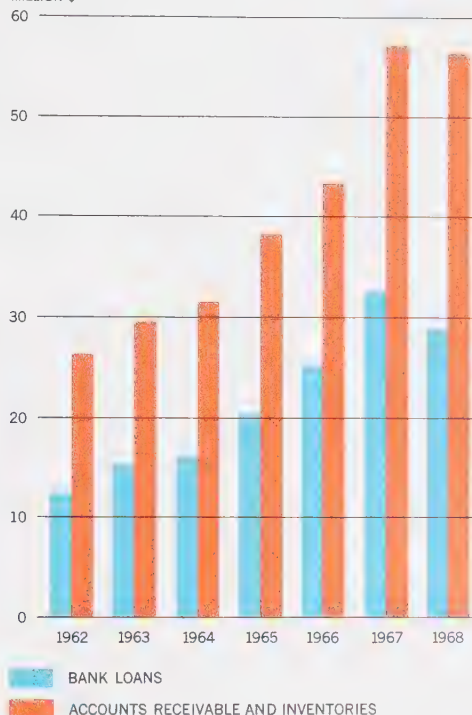
MILLION \$



Bank Loans compared to Accounts Receivable and Inventories

FINANCIAL YEARS ENDED JUNE 30

MILLION \$



Canadian Breweries Limited through Rothmans Investments Limited.

Bank Loans

Operating bank loans decreased from \$32,699,000 in 1967 to \$16,809,000 at June 30, 1968, mainly as a result of the issue of \$15,000,000 debentures.

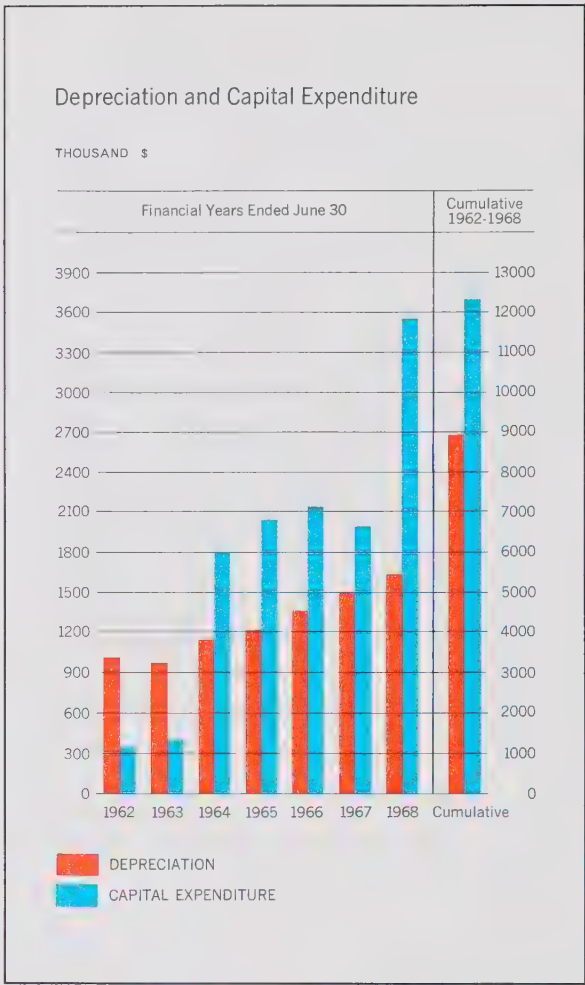
In addition, the Company borrowed \$12,000,000 for its investment in Rothmans Investments Limited, bringing total bank loans at June 30, 1968 to \$28,809,000.

Capital Expenditure

Net capital expenditure during the year under review amounted to \$3,564,000. This includes \$770,000 for the purchase of 33.8 acres of land at Dufferin Street and Steeles Avenue in Toronto, which the Company intends to use for another cigarette factory when required. An amount of \$610,000 was also spent during the year for the new warehouse in Quebec City.

Capital expenditure for the 1968/69 fiscal year has been budgeted at \$3,500,000; this includes an

unexpended amount of \$950,000 carried forward from the previous year.



REVENUE AND COSTS

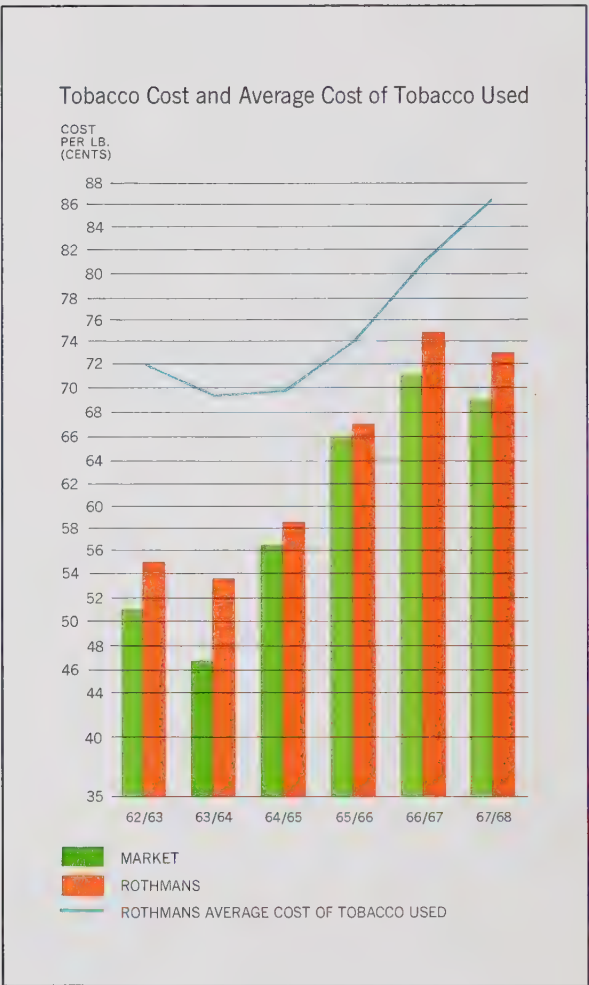
Sales and Earnings

The total increase in revenue to your Company, as a result of price changes during the year, amounted to \$7,850,000; of this amount, \$5,780,000 was absorbed by increases in sales and tobacco taxes. Increased operating costs also substantially offset the gains resulting from higher cigarette prices.

Tobacco

The cost of tobacco used increased by 6 cents per pound from 81 cents to 87 cents per pound.

Tobacco inventories at June 30, 1968 amounted to 39.4 million pounds valued at a cost of 87.0 cents per pound (1967: 39.7 million pounds—84.3 cents per pound).



Manufacturing and General Expenses

As shown in the Financial Statements, manufacturing and general expenses increased significantly

during the year. This increase includes higher labour costs as well as the total cost of developing and producing a cigarette with the Strickman Filter.

Depreciation

Depreciation for the year amounted to \$1,634,000, representing 16.4 percent of the net fixed assets at the 1968 year-end (1967: \$1,504,000 or 18.7 percent).

Interest

Interest paid during the year increased by \$498,000 from \$1,413,000 to \$1,911,000. This increase reflects higher interest rates in effect during the year. Interest paid this year also includes an amount of \$68,000 on the loan of \$12,000,000, which was utilized for your Company's investment in Rothmans Investments Limited.

Taxes

Federal Excise Taxes on cigarettes increased during the year by \$1.00 from \$5.00 to \$6.00 per thousand cigarettes.

Federal tobacco and sales taxes on a package of king size cigarettes are now as follows:

<i>Per Pack of:</i>	<i>20's</i>	<i>25's</i>
Excise Duty - - - - -	8.0¢	10.0¢
Excise Tax - - - - -	12.0¢	15.0¢
Sales Tax - - - - -	2.4¢	3.0¢
	<u>22.4¢</u>	<u>28.0¢</u>

In addition, Provincial taxes are as follows:

<i>Per Pack of:</i>	<i>20's</i>	<i>25's</i>
British Columbia	2¢	3¢
Alberta	Nil	Nil
Saskatchewan	7¢	8¢
Manitoba	8¢	10¢
Ontario	6¢	8¢
Quebec	8¢	10¢
New Brunswick	4¢	5¢
Nova Scotia	2¢	3¢
Prince Edward Island	8¢	10¢
Newfoundland	14¢	18¢

Income taxes charged against earnings in 1968 amounted to \$4,405,000 or 52.0 percent of earnings before tax. In the previous year, taxes amounted to \$3,949,000 or 51.2 percent of earnings before tax. This increase reflects the 3 percent surtax imposed on earnings effective January 1, 1968.

Total Costs

As in the previous year, the Consolidated Statement of Earnings this year includes a comprehensive breakdown of the Company's costs (Page 12).

Distribution of Sales Dollar

A chart outlining the main elements of costs as a percentage of total sales is given on Page 8 of this report.

Head Office: 75 DUFFLAW ROAD, TORONTO 19, ONTARIO

Auditors: PRICE WATERHOUSE & CO.

Bank: BANK OF MONTREAL

Registrar & Transfer Agent: THE ROYAL TRUST COMPANY

Solicitors: WAHN, MAYER, SMITH, CREBER, LYONS, TORRANCE & STEVENSON



SOME OTHER
BRANDS IN
OUR FAMILY
OF FINE
PRODUCTS





ROTHMANS OF PALL MALL CANADA LIMITED ANNUAL REPORT 1968

AR01



THE GREATEST NAME IN CIGARETTES

ROTHMANS REPORT TO SHAREHOLDERS
FOR THE SIX MONTHS ENDED DECEMBER 31, 1968
ROTHMANS OF PALL MALL CANADA LIMITED

To Our Shareholders:

Sales and earnings established new records for the six months ended December 31, 1968.

Earnings before income taxes increased by 14.4% to \$4,713,000 from \$4,120,000 in 1967. Net earnings for the same period increased by 2.3% to \$2,036,000 from \$1,990,000 in 1967 (per share: 1968—\$1.27, 1967—\$1.24). Interest charges for the 1968 period included an amount pertaining to the Company's investment in Canadian Breweries Limited, which is not deductible for tax purposes.

Sales increased by 11.4% to \$102,744,000 (1967: \$92,252,000). Unit cigarette sales increased from 5,627 million cigarettes to 5,887 million cigarettes, representing a gain of 4.6%. As mentioned in the review for the six months to December 31, 1967, year-end sales in 1967 were inflated due to increased buying by the trade as a result of anticipated price changes. Therefore, your Company's performance for the six months under review was better than the percentage figures indicate.

Industry production for the six months to December 31, 1968, as reported by the Dominion Bureau of Statistics, was 22,527 million cigarettes compared to 22,146 million cigarettes in 1967, an increase of 1.7%.

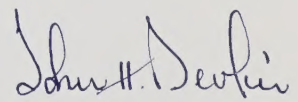
Our share of both the domestic and export cigarette markets continued to increase and sales for the six months to December 31, 1968, were 24% of the domestic and 32% of the

export markets. Due mainly to the very promising performance to date of the Company's new brands, Sportsman 68 mm. and Ransom, the marketing appropriation for the current year has been increased by more than \$1 million.

The average price paid by your Company for tobacco up to December 31, 1968 was 73.4¢ per pound compared to 69.5¢ for all tobacco sold. Your Company continues to pay premium prices for tobacco to ensure the high quality of its products.

On December 19, 1968, the Minister of Health announced the formation of a parliamentary committee to inquire into the aspects of smoking and health. While no agenda has been established, your Company's views will be submitted to this committee.

On January 27, 1969, the Company received the proceeds from the issue of \$20 million 6.85% Preferred shares, which will be utilized to finance the Company's investment in Canadian Breweries Limited and Larus & Brother Company. The issue carries warrants to purchase one Common share for each \$100 Preferred share.



President

January 31, 1969

ROTHMANS OF PALL MALL CANADA LIMITED

<i>Consolidated Statement of Earnings</i>	(Unaudited)		<u>Increase</u>
	6 months ended December 31, 1968	6 months ended December 31, 1967	
Sales—net.....	<u>\$102,744,000</u>	<u>\$92,252,000</u>	11.4%
Earnings before income taxes.....	\$ 4,713,000	\$ 4,120,000	14.4%
Estimated income taxes.....	<u>2,677,000</u>	<u>2,130,000</u>	25.7%
Net earnings for the period.....	<u>\$ 2,036,000</u>	<u>\$ 1,990,000</u>	2.3%
*Earnings per share (1.6 million common shares).....	<u>\$1.27</u>	<u>\$1.24</u>	

Consolidated Statement of Changes in Working Capital

Working capital was increased by:

Earnings for the period.....	\$ 2,036,000	\$ 1,990,000
Add/(deduct):		
Depreciation.....	859,000	754,000
Deferred income taxes and other.....	<u>(79,000)</u>	<u>71,000</u>
Funds from operations.....	<u>\$ 2,816,000</u>	<u>\$ 2,815,000</u>

Working capital was decreased by:

Fixed asset acquisitions—net.....	853,000	2,052,000
Dividends.....	800,000	—
Redemption of Class A shares.....	—	900,000
Refundable tax and other.....	<u>(50,000)</u>	<u>4,000</u>
	<u>\$ 1,603,000</u>	<u>\$ 2,956,000</u>
Increase/(decrease) in working capital.....	1,213,000	(141,000)
Working capital at beginning of the period.....	<u>15,971,000</u>	<u>12,271,000</u>
Working capital at end of the period.....	<u>\$ 17,184,000</u>	<u>\$12,130,000</u>

*Earnings per share of \$1.53 reported in 1967 were based on 1.3 million Common shares outstanding. As a result of the conversion of 300,000 class "B" Convertible Deferred shares into Common shares on June 30, 1968, the number of Common shares issued increased from 1.3 million to 1.6 million.



ROTHMANS OF PALL MALL CANADA LIMITED

DIRECTORS

JOEL WALKDON ALDRED

CHARLES FOWLER WILLIAMS BURNS

MAJOR GENERAL SIR FRANCIS DE GUINGAND,
K.B.E., C.B., D.S.O.

JOHN HERBERT DEVLIN

HAROLD SCANLON FOLEY

CHARLES ALBERT MASSEY

FREDERICK LAWRENCE PATTERSON

THE RIGHT HONOURABLE

LOUIS STEPHEN ST-LAURENT, P.C., C.C., Q.C., LL.D.

JOHN ELVIN SHAFFNER

WILMAT TENNYSON

OFFICERS

Chairman of the Board

THE RIGHT HONOURABLE

LOUIS STEPHEN ST-LAURENT, P.C., C.C., Q.C., LL.D.

President

JOHN HERBERT DEVLIN

Vice President Marketing

WILMAT TENNYSON

Vice President Finance and Treasurer

PAUL JACOBUS ERASMUS

Vice President and Secretary

ROBERT HOWIE HAWKES

Vice President Production

DANIEL DI IANNI

Vice President Personnel and Industrial Relations

GEORGE STEWART

Vice President Sales

ROBERT THOMAS LLOYD

Vice President Advertising

ROY HENRY NEWTON